

***United States Court of Appeals
for the Second Circuit***



**BRIEF FOR
APPELLANT**

ORIGINAL

77-7009

IN THE
United States Court of Appeals
For The Second Circuit

WILLIAM R. VAN GEMERT, ALBERT A. HENNING, EDWARD E. HOUCHINS, NATHAN PEARLMAN, ELIAS A. CHARIOTT, CHARLES K. DAVIS, ANDREAL HOLDING CORP., SAMUEL A. WEISS, IRWIN L. ISERT, JACK KIRSCHNER, CHARLES FRIEDMAN, H. MICHAEL ALBERS, ABRAHAM STERN, EDWARD KEMPLER, SIMEON A. SCHLOSS, JR., MARY JANE SCHLOSS SILVERMAN, SIMEON A. SCHLOSS, JR., and MARY JANE SILVERMAN, Trustees under the Last Will and Testament of Floretta Schloss Wile, DAVID M. BOTSFORD, MRS. SAMUEL LEMLER, LOUIS DAVIS, MRS. LEONARD C. DILL, JR., JOSEPH SCHLAGMAN, NATALIE K. WIGLER, ANN LOUISE DIAMOND, SAMUEL CHARDAYVOYNE, WILLIAM M. JONES, MR. & MRS. H. DIENEMAN, MILTON HART, MARY LEVIN, FRANCES DAVIS, E. JULIAN DAVIS, ROBERT LEMLICH, ARTHUR FRISCH, MARIAN S. MITCHELL, VINCENTE J. BONNARD, HAROLD M. WHITE and MARGARET C. WHITE, MORRIS BERNSTEIN, WALTER L. EATON, ERNEST G. ANGEVINE, ABRAHAM PERCHICK, COMMITTEE FOR THE ESTATE OF MAX SCHNEIDER, an incompetent, FRANCIS H. SHOUBE, and ALBERT A. ARDITTI, GERTRUDE McNAUGHT, MRS. J. H. STEIN, JOAN S. BERMAN, J. DAVID STEIN, SARAH E. MORITZ, VIRGINIA W. STAUB, LOUIS BERGLAS, DR. JACK DIENER, DENNIS J. FINN, BERTHA J. WINER, JOANNE W. FINN and S. EDWARD MITTLER, for and in behalf of themselves and for all other holders of the BOEING COMPANY 4½% Convertible Subordinated Debentures, due July 1, 1980 who are similarly situated,

Plaintiffs-Appellants,

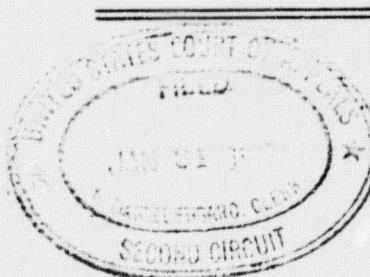
vs.

THE BOEING COMPANY (formerly BOEING AIRPLANE COMPANY), CLAIRMONT L. EGTVEDT, WILLIAM M. ALLEN, EDWARD C. WELLS, JAMES E. PRINCE, LOWELL P. MICKELWAIT, W. L. CAMPBELL, ARTEMUS L. GATES, CRAWFORD H. GREENEWALT, WILLIAM G. REED, D.E. SKINNER, THOMAS R. WILCOX, JOHN O. YEASTING and GEORGE H. WEYERHAEUSER,

Defendants-Appellees.

ON APPEAL FROM JUDGMENT OF THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK.

BRIEF FOR PLAINTIFFS-APPELLANTS



KASS, GOODKIND, WECHSLER &
GERSTEIN

Attorneys for Plaintiffs-Appellants,
William R. Van Gemert, Albert A.
Henning, Edward E. Houchins,
Nathan Pearlman, Elias A. Chariott
122 East 42nd Street
New York, New York 10017
(212) 867-8570

TABLE OF CONTENTS

	<u>Page</u>
TABLE OF AUTHORITIES	(i)
ISSUES	1
STATEMENT OF THE CASE	4
A. Nature of the Action and Prior Proceedings.	4
B. The Decision and Order of the District Court With Respect to Damages And the Facts Pertaining Thereto.	5
ARGUMENT	7
POINT I - AN AWARD OF PREJUDGMENT INTEREST IS MANDATORY BECAUSE THE CASE WAS DECIDED UNDER THE LAWS OF NEW YORK STATE AND UNDER SUCH STATE LAW, PRE- JUDGMENT INTEREST IS MANDATORY. MOREOVER, EVEN IF IT IS ASSUMED THAT THE AWARD OF INTEREST WAS DISCRETIONARY, NOT AWARDING INTEREST IN THIS CASE WAS AN ABUSE OF DISCRETION.	7
POINT II - THE MEASURE OF DAMAGES SHOULD HAVE BEEN BASED UPON THE COST TO THE CLASS OF REPLACING THEIR BOEING STOCK WHEN THE MARKET VALUE WAS HIGHEST WITHIN A REASONABLE TIME AFTER CONVERSION PRIVILEGES WERE CUT OFF .	10
POINT III - THE ORDER SHOULD BE MODIFIED TO PROVIDE THAT THE AMOUNT OF THE LOSS NOT CLAIMED BY MEMBERS OF THE CLASS IS TO BE DISTRIBUTED AMONG THOSE WHO DO MAKE CLAIM .	14
CONCLUSION	16

TABLE OF AUTHORITIES

<u>Cases</u>	<u>Page</u>
<u>Bott v. American Hydrocarbon Corp.</u> , 458 F. 2d 229 (5th Cir. 1972)	7
<u>Gelb v. Zimet Brothers, Inc.</u> , 34 Misc. 2d 401, <u>aff'd</u> 18 A.D. 2d 1967	12
<u>Hartford Accident & Indemnity Co. v. Walston & Co.</u> , 22 N.Y. 2d 672 (1968)	11
<u>Jones v. National Chautaugua County Bank of Jamestown</u> , 272 App. Div. 521	11, 12
<u>Joseph v. Sulzberg</u> , 136 A.D. 499 (1910)	13
<u>Komie v. Buehler Corp.</u> , 449 F. 2d 644 (9th Cir. 1971)	7
<u>Mayer v. Momzo</u> , 221 N.Y. 442 (1917)	11, 12
<u>McDonnel Douglas Corp. v. Polin</u> , 429 F. 2d 30 (3rd Cir. 1970)	7
<u>National Dairy Products v. Lawrence Field Warehousing Corp.</u> , 22 A.D. 2d 420	11
<u>Peterson v. Kloss</u> , 433 F. 2d 911 (5th Cir. 1970)	7
<u>Statutes and Rules</u>	
CPLR 5001(a)	7, 8
FRCP 23(b) (1) & (2)	14

UNITED STATES COURT OF APPEALS
SECOND CIRCUIT

-----X
VAN GEMERT, et al.,

Plaintiffs-Appellants,

-against-

THE BOEING COMPANY, et al.,

Defendant-Respondent.
-----X

APPELLANTS' BRIEF

ISSUES

1. When liability is determined on the grounds of state law, and the District Court has jurisdiction thereover upon the principles of pendent jurisdiction, should the law of the state with respect to the awarding of prejudgment interest be followed?

The Court below answered in the negative. Appellants respectfully submit that this issue should have been answered in the affirmative.

2. Under the law of New York State, is the award of prejudgment interest mandatory on a judgment arising from plaintiffs' loss of conversion privileges on convertible debentures, by reason of defendants' failure to provide

adequate and reasonable notice of a call?

The court below answered in the negative. Appellants respectfully submit that this issue should have been answered in the affirmative.

3. When it has been determined that defendants, 11 years ago, violated the law to the damage of the plaintiffs, and that plaintiffs have been entitled to become compensated for such damages since such violation 11 years ago, and the defendants have been able to obtain millions of dollars in interest on such damages over said 11 years but plaintiffs have not been able to obtain such interest because judgment for such damages had not been obtained until the expiration of said 11 years, is it an abuse of discretion to refuse to award plaintiffs such interest as part of the judgment?

The court below answered in the negative. Appellants respectfully submit that this issue should have been answered in the affirmative.

4. When holders of convertible debentures lose their right to convert because the corporation violated the law in failing to provide adequate notice that conversion rights were about to be cut off, are the damages to the debenture holders based upon the market value of the securities into which the debentures were convertible at the date conversion rights were cut off, or at the date that the

market value was highest during the subsequent period within which the debenture holders could reasonably be expected to purchase securities on the market?

The court below held that the market value on the date that conversion rights were cut off is determinative of damages. Appellants respectfully submit that the subsequent date should be determinative.

5. In a class action, where it is determined that defendants violated the law causing a loss to the class in a specific aggregate amount and judgment is awarded in favor of the class for such amount, should the amount of the loss not claimed by members of the class be distributed among those who do make claim or retained by the defendants?

The court below did not reach this issue. Appellants respectfully submit that such unclaimed loss should be distributed among those members of the class who make claim.

STATEMENT OF THE CASE

A. Nature of the Action and Prior Proceedings

This is a class action involving a call by defendant The Boeing Company ("Boeing") of convertible debentures listed on the New York Stock Exchange ("Exchange"). The action was brought on behalf of debenture holders who did not receive notice of the call and, as a result, failed to convert their debentures into common stock of Boeing before their rights to do so were cut off, pursuant to the call, on March 29, 1966. While Boeing may have complied with the formal notice requirements of the indenture with respect to the call, it did not comply with the rules of the Exchange and with its listing agreement with respect thereto. Since Exchange rules were promulgated pursuant to the Securities Exchange Act of 1934 (the "Act"), the plaintiffs contend that, inter alia, Boeing's failure to comply with the Exchange rules was actionable under the Act.

The District Court had held that Boeing had not violated the Act and, if it had, the violation was not civilly actionable. The District Court accordingly dismissed the complaint.

This court reversed and remanded for a determination of damages. In its opinion, this court discussed plaintiffs' claim that Boeing's violation of the Exchange

rules constituted an actionable federal claim under the Act, but decided only that the claim "is sufficient for jurisdictional purposes in any event", i.e., that such claim was sufficient for its exercise of pendent jurisdiction over violations of state law (A 105) . This court then decided in favor of the plaintiffs on the grounds that state law had been violated because the notice of the call was inadequate and unreasonable (A 106-112), and remanded for a determination of damages. It is the district court's determination of such damages which is the subject of the instant appeal.

B. The Decision And Order of the District Court With Respect To Damages And The Facts Pertaining Thereto.

The District Court fixed the aggregate damages to the class at \$3,289,359. In doing so, it (1) expressly refused to award prejudgment interest to the class, (2) calculated damages based upon the market value of Boeing stock at the time the conversion privileges were cut off rather than upon the market value at a time when the members of the class could reasonably have replaced their loss in the market, and (3) failed to address the question as to what happens to any portion of the damages attributable to class members who cannot be located and/or make no claim for their share.*

* The District Court rejected a contention by Boeing that all those members of the class who had redeemed their debentures during the pendency of the litigation waived their right to recover. However, Boeing has filed no notice of appeal and, therefore, such contention is not at issue here. Appellants agree fully with the District Court's reasoning, set forth in its opinion, in rejecting Boeing's waiver contention and refer this court thereto if required on this appeal for any reason. (A 354-357)

On March 29, 1966, the date conversion privileges were cut off, \$100 of principal amount of debentures was convertible into \$316.25 of stock (A 121). As shown in the affidavit in support of plaintiffs' motion for fixing damages, the damages, excluding interest, based upon the market value of Boeing stock on that date, is the \$3,289,359 adopted by the District Court (A122). However, within 30 days after the cutoff date, the same amount of Boeing stock rose to \$364. Based upon this higher value, the damages, exclusive of interest, amounts to \$4,026,762.25 (A 121, 122). The court however, would not consider damages based upon this later date but decreed damages based upon the market value of Boeing stock on the date conversion privileges were cut off.

Prejudgment interest would be, to say the least, an extremely significant amount. On the amount of \$3,289,359 awarded by the District Court, interest from April 1, 1966 to February, 1977, based upon the prevailing legal rates of interest in New York over the period involved, would be \$2,556,489.72. On the amount of \$4,026,762.25, the interest would be \$3,129,599.62. Despite the fact that Boeing had utilization of the funds throughout the 11 years of litigation in this matter, and thereby had the opportunity to obtain the millions of dollars in interest involved, at the expense of the class, the District Court refused to award interest to the class.

ARGUMENT

POINT I

AN AWARD OF PREJUDGMENT INTEREST IS MANDATORY BECAUSE THE CASE WAS DECIDED UNDER THE LAWS OF NEW YORK STATE AND, UNDER SUCH STATE LAW, PREJUDGMENT INTEREST IS MANDATORY. MOREOVER, EVEN IF IT IS ASSUMED THAT THE AWARD OF INTEREST WAS DISCRETIONARY, NOT AWARDING INTEREST IN THIS CASE WAS AN ABUSE OF DISCRETION.

In determining the prejudgment interest the plaintiff is entitled to upon any state claim brought in federal court, the federal courts looked to the applicable state law. Bott v. American Hydrocarbon Corp., 458 F. 2d 229 (5th Cir. 1972); Komie v. Buehler Corp., 449 F. 2d 644 (9th Cir. 1971); McDonnell Douglas Corp. v. Polin, 429 F. 2d 30 (3rd Cir. 1970); Peterson v. Kloss, 433 F. 2d 911 (5th Cir. 1970). Since New York State law was made applicable by an express provision of the indenture*, New York law as to the allowance of prejudgment interest governs.

New York law as to the allowance of prejudgment interest is clear. Section 5001(a) of the Civil Practice Law and Rules provides that prejudgment interest is recoverable upon all but personal injury claims, i.e., upon contract and property actions, as follows:

* Section 17.04 of the Debenture states "Law of New York State to govern. This indenture and each debenture shall be deemed to be a contract made under the laws of the State of New York and shall be construed for all purposes in accordance with the laws of said state". (A 51)

"Interest shall be recovered upon a sum awarded because of a breach of performance of a contract, or because of an act or omission depriving or otherwise interfering with title to, or possession or enjoyment of of, property...".

Section 5001(b) of the Civil Practice Law and Rules provides that the interest shall be computed from the earliest date the cause of action existed.

The District Court ignored the mandatory requirements for awarding prejudgment interest under New York State law, by holding that the action was decided upon a violation of the Federal Securities Act rather than upon a violation of state law. However, as shown above, this court, in reversing and remanding to the District Court, expressly held only that the federal claim was valid for jurisdictional purposes, and then found liability upon the basis that the notice of call was inadequate and unreasonable under the pendent state claims. Thus, the District Court's statement that this court's reversal rests upon a finding that Boeing ran afoul of the Securities Act, is simply wrong and contrary to the express wording of this court's opinion.

The District Court also purported to avoid the clear mandate of state law, that interest be awarded, with the statement that, "even if state law applies, as the indenture provided, the award of interest is discretionary in that it would be inequitable to award interest on a claim which could not have been reasonably anticipated ... when

[Boeing] gave the notice required by the indenture". Putting aside the question as to whether or not the award of interest would be equitable, the above quoted portion of the CPLR renders prejudgment interest mandatory regardless of the equities. Thus, upon the District Court's assumption that state law does apply, it was required to award prejudgment interest even if plaintiffs were to concede, arguendo, that the equities with respect thereto were with Boeing.

The equities with respect to the award of prejudgment interest are, however, exactly contrary to that espoused by the District Court. Regardless of whether or not Boeing could have anticipated the liability when it violated the law, it still had the use of the plaintiffs' money for almost 11 years at the expense of the class. During all that time, the class had the right to its recovery and it, rather than Boeing, is now entitled to the proceeds from the use of the money. Therefore, even if it is assumed, arguendo, that the award of interest is discretionary, and not mandatory, the District Court's refusal to award interest is an abuse of such discretion.

There is no basis whatsoever for permitting Boeing to profit from the delay in the adjudication of the class' rights, at the class' expense. In exercising its discretion against the award of interest, the District Court referred to the "punitive effect of an award of interest because of

the absence of any illegal profits enuring to the defendants". However, the award of interest is not punitive, but is compensatory and required to place the class in the position that it would have been had it received notice of the call, converted before the cutoff date, and earned interest on the value of the stock into which the bonds were convertible. "[I]llegal profits" have enured to the defendants in that Boeing has obtained the interest on funds rightfully belonging to the class. Accordingly, the District Court had no basis whatsoever in exercising discretion against the award of prejudgment interest and, therefore, the exercise of such discretion was abusive.

POINT II

THE MEASURE OF DAMAGES SHOULD HAVE BEEN BASED UPON THE COST TO THE CLASS OF REPLACING THEIR BOEING STOCK WHEN THE MARKET VALUE WAS HIGHEST WITHIN A REASONABLE TIME AFTER CONVERSION PRIVILEGES WERE CUT OFF

Boeing's violation of state law constitutes a conversion of the class member's rights to the stock into which their debentures were convertible and/or a breach of contract arising from the debenture. As will be shown below, the amount of the resulting damages is the same whether Boeing's violation is based upon conversion or breach of contract. In both cases, the damages are calculated upon the cost to the class of replacing this stock within a

reasonable time after conversion privileges were cut off, and not merely upon the market value of the stock at the cutoff date as insisted upon by the District Court.

Under New York law the failure to deliver stock in which another has rights constitutes a conversion thereof. Mayer v. Momzo, 221 N.Y. 442 (1917); Hartford Accident & Indemnity Company v. Walston & Co., 22 N.Y. 2d 672 (1968). As stated in the Mayer case, when the defendant broker sold stock from plaintiff's margin account:

"We think that the sale of the stock under the circumstances amounted to a conversion." 221 N.Y. 444, 445

Since Boeing did not deliver the stock available upon conversion of the debentures to the class members, and took steps to deprive them of such stock by providing inadequate notice of the call, Boeing's violation constituted a conversion.

When property having a stable market value is converted, damages are generally based upon the market value of the converted property at the time of the conversion. National Dairy Products v. Lawrence Field Warehousing Corp., 22 A.D. 2d 420; Jones v. National Chautaugua County Bank of Jamestown, 272 App. Div. 521. However, when the converted property has a fluctuating value, such as securities do, the damages are based upon the highest market value of the

property within a reasonable time after the conversion is learned of by the plaintiff. Jones v. National Chautaugua County Bank of Jamestown, supra; Gelb v. Zimet Brothers, Inc., 34 Misc. 2d 401, aff'd 18 A.D. 2d 1967; Mayer v. Momzo, supra.

As stated in the Mayer case, supra:

"The rule is that a person whose stocks have been converted is entitled to a reasonable time after notice of the conversion with which to determine whether he would purchase other stocks in the place thereof and that he may use as a basis for his claims as damages resulting from the conversion the highest prices which have prevailed during such reasonable period (Baker v. Drake, 53 N.Y. 221). It has been held under varying circumstances that 30 days or 15 days or 60 days would be such reasonable period* (Colt v. Owens, 90 N.Y. 368; Wright v. Bank of Metropolis, 110 N.Y. 237; Minor v. Berveridge, 141 N.Y. 399; Mullen v. Quelin & Co., 195 N.Y. 109) (221 N.Y. 442, 446-447)" (Emphasis Added)

* The date of the highest market price within 30 days from the cutoff date utilized to determine the damages, urged as appropriate herein, occurred on April 14, 1966, i.e., 16 days after the cutoff date. This was agreed upon in paragraph 148 of a stipulation of agreed facts contained in the record on appeal. As shown in the affidavit submitted in support for the determination of damages, the market value of Boeing stock on that day was \$365 per \$100 of principal amount of the debentures. Based thereon, the principal amount of the damage to the class is \$4,026,762.25. (A)

If Boeing's violation is deemed a breach of the contract arising from the debentures, rather than a conversion, the results would still be the same. The breach of a contract would have prevented the plaintiffs from obtaining the more valuable stock until such time as they could reasonably have replaced same by purchasing stock on the market. In Joseph v. Sulzberg, 136 A.D. 499 (1910), the parties had stipulated that the measure of damages was to be based upon a contractual obligation rather than a conversion, and the court held that the plaintiff had failed to make out a cause of action for a breach but stated that, if he had, the measure of damages would have been the same as in conversion. The court stated:

"The subject of the contract alleged in the complaint was stock of an incorporated company, and the damages ordinarily allowed for the breach of a contract to buy or sell such stock is the difference between the price stated in the contract and the price in which the same stock could be sold in the market within a reasonable time after breach."

From the foregoing, it is seen that, regardless of the nature of Boeing's violation, the measure of damages is based upon the ability of the plaintiffs to replace their loss in the market and, therefore, the higher principal amount of damages of \$4,026,762.25 should have been awarded rather than the lower amount based upon the market value of Boeing stock at the cutoff date.

POINT III

THE ORDER SHOULD BE MODIFIED TO PROVIDE THAT THE AMOUNT OF THE LOSS NOT CLAIMED BY MEMBERS OF THE CLASS IS TO BE DISTRIBUTED AMONG THOSE WHO DO MAKE CLAIM.

Although the District Court decreed that damages to the class were in a specific amount, it made no mention as to what would happen to any portion of such damages not claimed by members of the class. Boeing has contended that it should simply be able to keep any unclaimed portion of the damages and thereby obtain a bonanza to the extent of such unclaimed damages. However, there is no precedent, reason, logic or justice in allowing Boeing to escape any portion of its liability in this manner.

The District Court expressly determined that the class was being maintained under Rule 23(b)(1) and (2), rather than 23(b)(3), in order to prevent inconsistent or variant adjudications with respect to individual members of the class. (A70-75) The court stated, at the hearing resulting in the class adjudication, that by defining the class as one under Rule 23(b)(1) and (2),

"...everybody that is a member of the class would be bound by this judgment. Everybody who is a member of the class will get the benefits."

Thus, the intent and purpose of the class involved here, is such that full payment is to be made for the loss incurred and that there be no fragmentation of any judgment based upon particular actions of members of the class. To be consistent

with such intent and purpose, Boeing must pay the full loss and cannot benefit if some members of the class fail to participate.

This is a class action and damages are awarded against Boeing and in favor of the class. Whether or not all members of the class participate in the recovery is an internal affair of the class, and should be of no concern to Boeing and in no way effect the amount of money which it must pay to the class for the injury sustained by it. Therefore, the full amount of the loss should be payable to the class, regardless of what percentage of the class eventually makes claim, and then such amount should be distributed among the participating members of the class.

While there is no reason to permit Boeing the bonanza of any portion of the damages attributable to unclaiming class members, there are sound equitable reasons for distributing the unclaimed portion of the damages among the members who do make claim. Class members may well have to pay cost and legal fees of this action and, therefore, may not be made whole. Those members of the class who are sufficiently interested in the benefits should also share in the unclaimed portion, even if for no other reason than to enable them to recover their fees and costs and thereby more nearly be made whole.

CONCLUSION

For the reasons stated above, the order of the District Court should be modified to the extent of (1) awarding damages in the principal amount of \$4,026,762.25, (2) awarding prejudgment interest on said amount from April 1, 1966 and (3) directing that any unclaimed portion of the damages be distributed among the members of the class who have made claim.

Respectfully submitted,

KASS, GOODKIND, WECHSLER & GERSTEIN
Attorneys for Appellants Van Gemert,
Henning, Houchins, Pearlman and
Chariott

OF COUNSEL:

Stuart D. Wechsler

Service of ^{Two} ~~three~~ copies of the within
is admitted this 31st day of January 1977

Davis Polk

Attorneys for Appellees

Nathan Mannheim, Esq., Walter Friedman

W. M. By Norman Davis

As Attorneys for Committee for Plaintiffs-Appellants

Irving Steiner

Irving Steiner

As Attorneys for Committee for Plaintiffs-Appellants

